

Order 2004-2-14
Served: February 20, 2004



UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY
WASHINGTON, D.C.

Issued by the Department of Transportation
on the **17th day of February, 2004**

Essential Air Service at

MANHATTAN, KANSAS
SALINA, KANSAS

under 49 U.S.C. 41731 *et seq.*

Docket OST-2003-15483
Docket OST-2002-11376

ORDER SELECTING CARRIER

Summary

By this order, the Department is selecting Air Midwest, Inc., a wholly-owned subsidiary of Mesa Air Group, Inc., d/b/a US Airways Express (Air Midwest), to provide subsidized essential air service (EAS) for a two-year period at Manhattan and Salina, Kansas, at a combined annual subsidy rate of \$721,605. (See Appendix A for an area map.)

Background

On January 23, 2002, Air Midwest filed a 90-day notice of its intent to suspend its unsubsidized scheduled air service at Salina. In response, we issued Order 2002-3-31 requesting proposals for replacement service and requiring the carrier to continue to serve the community while we processed a carrier-selection case.¹ While we were in the process of negotiating a subsidy rate with Air Midwest, the only applicant, on June 20, 2003, the carrier filed a 90-day notice to suspend service at Manhattan, the intermediate stop on the Salina-Manhattan-Kansas City routing. Because the Salina and Manhattan cases were inextricably linked, by Order 2003-8-23, August 21, 2003, we deferred action

¹ Order 2002-3-31 required Air Midwest to continue its current service at Salina consisting of 18 one-stop (via Manhattan) round trips per week to Kansas City using 19-seat Beech 1900D aircraft.

on a carrier-selection decision while we processed the Manhattan case, and set a short-term subsidy rate in order for Air Midwest to be paid during this period.²

In the meantime, at Manhattan the Department issued Order 2003-9-17, which prohibited Air Midwest from suspending service beyond the end of its 90-day notice period and requested proposals from carriers interested in providing replacement service in the Manhattan–Kansas City market. In response to our request, we received proposals from two carriers, the incumbent carrier, Air Midwest and a new carrier, Multi-Aero, Inc, d/b/a Air Choice One (Multi-Aero). Currently, Air Midwest is the only carrier serving Salina and Manhattan, providing three round trips to Kansas City International Airport each weekday and weekend with 19-seat, Beech 1900D turboprop aircraft, over a Salina–Manhattan–Kansas City itinerary, operating as US Airways Express.

Proposals

Air Midwest’s proposal consists of four options, although two are essentially identical, except for the manner in which the subsidy rate is constructed.³ Its Options 1 and 3 would both provide three round trips on weekdays and weekends over a Salina-Manhattan-Kansas City routing -- Option 1 for \$786,611 and Option 3 for \$721,605. Its Options 2 and 4 would provide the same three round trips a day over the Salina-Manhattan-Kansas City routing *plus* a fourth Manhattan – Kansas City round trip a day -- Option 2 for \$924,068 and Option 4 for \$874,432. Air Midwest has a code-share agreement with US Airways and would continue to serve Manhattan and Salina under all four options as a US Airways Express carrier using 19-seat Beech 1900D aircraft.

Multi-Aero proposes to provide scheduled passenger service as a commuter air carrier operating under Federal Air Regulation (FAR) Part 135.⁴ Multi-Aero’s proposal would provide Manhattan with five nonstop round trips per day to Kansas City International Airport using 19-seat aircraft configured with 14 passenger seats.⁵ While Multi-Aero’s proposal indicates that it can serve Manhattan without subsidy, it does indicate that it

² Air Midwest agreed to provide Salina with three one-stop round trips per day to Kansas City for an annual subsidy rate of \$536,237 as a final, short-term rate from April 1, 2003, until we concluded a long-term carrier selection proceeding. That rate, set by Order 2003-8-23, was based on providing service in the Salina – Manhattan market only, since Air Midwest was, at the time, already providing Manhattan–Kansas City service on a subsidy-free basis.

³ The differences in subsidy rates for the same service levels stem from the way Air Midwest constructs the rates. Under its Options 1 and 2, Air Midwest constructs the Manhattan-Kansas City piece of the rate and adds it to the existing Salina-Manhattan \$536,237 rate, whereas for its Options 3 and 4, it costs out the whole route stating that, “The combined bids are slightly less expensive because the 2 cities combined more fully utilize the aircraft.”

⁴ Multi-Aero indicates in its application that it has a 20 plus-year history of providing on-demand, air taxi service under Federal Air Regulation (FAR) Part 135, but is still in the process of obtaining authority from the Department to provide scheduled service under Part 135 as a commuter carrier.

⁵ Carriers providing scheduled service under FAR Part 135 are limited to using aircraft configured with nine or fewer passenger seats. To operate as a scheduled carrier using aircraft configured with 10 or more passenger seats, a carrier must be certified by the Federal Aviation Administration to operate under FAR Part 121. Although Multi-Aero indicated that it would use 19-seat aircraft, configured with just 14 seats, it did not indicate what type of aircraft it would use.

would need \$137,236 from the Small Community Air Service Development Pilot Program (SCASDPP) grant that the community received in October 2002.⁶ The carrier did not indicate that it has a code-share relationship with any carrier serving Kansas City International Airport.

Community Comments

Civic leaders in both Salina and Manhattan indicated their support for Air Midwest in letters dated December 22, 2003, and January 7, 2004, respectively. The Mayor and the Chairman of the Salina Airport Authority, supported by the Salina Area Chamber of Commerce, favor Air Midwest's four-round-trip option (Option 4). Notably, they mentioned that on October 9, 2003, Air Midwest announced a new lower point-to-point fare proposal that they believed, would "enable the airline to regain passengers lost in recent years and is another step in a rebuilding process Air Midwest is committed to." Their letter also mentioned that the financial strength of Air Midwest's parent, Mesa Air Group, had enabled the carrier "to continue service through hard economic times." Manhattan officials reiterated the community's long-standing relationship with Air Midwest and "would anticipate the continuation of a positive relationship in the future." They did, however, express "some reservations" regarding service frequency, fares, and the timing of connecting flights, as most Manhattan passengers use Kansas City "as an access point to the nation's air transportation network, as opposed to Kansas City as a destination point." Also, in a letter dated January 14, 2004, the Manhattan airport manager mentioned that the Manhattan City Commission had recommended that Air Midwest be designated as the community's EAS provider and that a portion of the SCASDPP grant be utilized by Multi-Aero or another carrier to provide additional service from Manhattan to Kansas City.

Decision

We have decided to select Air Midwest to provide subsidized EAS at Manhattan and Salina for the two-year period beginning on the first day of the month following the service date of this order. In selecting a carrier to provide subsidized essential air service, 49 U.S.C. 41733(c)(1) directs us to consider four factors: (a) the carriers' demonstrated service reliability; (b) the carriers' contractual and marketing arrangements with a larger carrier at the hub; (c) the carriers' interline arrangements with a larger carrier at the hub; and (d) community views. In addition, we have always given weight to the applicants' relative subsidy requirements.

In this case, all of the statutorily required selection criteria point toward the selection of Air Midwest. First, both communities prefer the selection of Air Midwest. Second, Air Midwest provides service to both Salina and Manhattan under a code-share arrangement with US Airways at Kansas City International that offers beyond-hub benefits such as one-stop check in, interline baggage handling, through ticketing, and joint fares. Also, the carrier has recently informed the community that it now has a code-share relationship with

⁶ The SCASDPP is also administered by the Department.

United Air Lines at Kansas City, further improving connecting opportunities and on-line services. Moreover, Air Midwest has operated for many years as a scheduled carrier in general and, specifically, at these two communities. Multi-Aero, on the other hand, has no community support, does not have contractual or marketing arrangements with a major carrier at the hub, and has no demonstrated service reliability in providing scheduled air service -- all statutory criteria.⁷

In addition to the statutorily required carrier selection criteria, fiscal prudence requires that we consider the relative subsidy requirements, as we have done since the inception of the program. In that regard, any overall subsidy savings of selecting Multi-Aero would be relatively small, or very possibly, nonexistent.

Air Midwest's subsidy request for Salina and Manhattan combined is \$721,605. That includes its current rate of \$536,237 for serving Salina, meaning that the implicit cost of serving Manhattan is a relatively modest \$185,368. Further, if we were to select Multi-Aero to serve Manhattan, the cost of securing Salina's EAS would likely increase -- perhaps considerably. The current subsidy of \$536,237 covers only the costs of Air Midwest's operating the 58-mile Salina-Manhattan segment. The subsidy costs of flying the nonstop 161-mile Salina-Kansas City route could be far greater than the current rate of \$536,237, and likely even greater than the combined rate of \$721,605 for service to both communities. Thus, the selection of Multi-Aero to serve Manhattan would result in minimal subsidy savings, and might even require *more* subsidy than Air Midwest's proposal to serve Salina and Manhattan together over a Salina-Manhattan-Kansas City routing.

We also share the communities' concerns about Multi-Aero's ability to maintain operations with no EAS subsidy, even with funds from the SCASDPP. In particular, Multi-Aero's zero subsidy proposal is premised on traffic projections of 31,500, almost double those generated in 2002 (18,600), and almost three times above those generated by the community in 2003 (31,500 compared to 11,970). We recognize that Multi-Aero's passenger projections are based on more frequencies than Air Midwest has recently provided, but it has no track record upon which to base its projections, it does not have the ability to attract passengers through a code-share relationship with a major carrier, nor make connections on a single ticket to destinations beyond Kansas City. We have no reason to believe that Multi-Aero's service to Kansas City would be markedly more attractive than Air Midwest's has been, and we are therefore skeptical that the carrier's projections could be attained even by the end of the rate term, much less that they represent an annual average during that term. To the extent that Multi-Aero may overestimate traffic, it would correspondingly also overestimate revenues and underestimate its subsidy requirement. Because of this, we are simply not confident that

⁷ Multi-Aero recently applied for a second extension to delay commencing the start-up of scheduled commuter operations until at least March 31, 2004. That request is currently under review by the Department. See Extension Request in Docket OST-2002-12417, filed December 16, 2003.

the carrier could operate throughout the two-year term without some erosion or disruption of service.

Thus, based on all of the above, we have decided to select Air Midwest to serve Salina and Manhattan for a new two-year period at the proposed annual subsidy of \$721,605 (Option 3) to provide three nonstop round trips on weekdays and on weekends to Kansas City over a Salina – Manhattan – Kansas City routing with 19-seat Beech 1900D turboprop aircraft. Since the carrier is already serving the markets at issue, the effective date of the two-year period will be the first day of the month following the service date of this order.

Carrier Fitness

49 U.S.C. 41737(b) and 41738 require that we find an air carrier fit, willing, and able to provide reliable service before we may subsidize it to provide essential air service. Air Midwest was most recently found fit to provide scheduled passenger service by Order 2003-10-28, selecting the carrier to provide EAS at Dodge City, Garden City, Great Bend, and Liberal, Kansas. Since that time, no information has come to our attention that would lead us to question the carrier's ability to operate in a reliable manner. The FAA has advised us that the carrier is conducting its operations in accordance with its regulations, and knows of no reason why we should not find that Air Midwest is fit. Based on the above, we find that Air Midwest is fit to provide the essential air transportation at issue in this case.

This order is issued under authority delegated in 49 CFR 1.56a(f).

ACCORDINGLY,

1. The Department selects Air Midwest, Inc., d/b/a US Airways Express, to provide essential air service at Salina and Manhattan, Kansas, as described in Appendix B for the two-year period beginning on the first day of the month following the service date of this order;
2. The Department terminates the rate of compensation for Air Midwest, Inc., d/b/a US Airways Express, for the provision of essential air service at Salina, Kansas, as set by Order 2003-8-23, effective on the first day of the month following the service date of this order;
3. The Department sets the final rate of compensation for Air Midwest, Inc., d/b/a US Airways Express, for the provision of essential air service at Salina and Manhattan, Kansas, as described in Appendix B for the two-year period described above, payable as follows: for each calendar month during which essential air service is provided, the amount of compensation shall be subject to the weekly ceiling set forth by Appendix B

and shall be determined by multiplying the subsidy-eligible flights each way completed during the month by \$200.78;⁸

4. The Department directs Air Midwest, Inc., d/b/a US Airways Express, to retain all books, records, and other source and summary documentation to support claims for payment, and to preserve and maintain such documentation in a manner that readily permits its audit and examination by representatives of the Department. Such documentation shall be retained for seven years or until the Department indicates that the records may be destroyed, whichever comes earlier. Copies of flight logs for aircraft sold or disposed of must be retained. The carriers may forfeit its compensation for any claim that is not supported under the terms of this order;

5. We find that Air Midwest, Inc., d/b/a US Airways Express, continues to be fit, willing and able to operate as a certificated air carrier and capable of providing reliable essential air service at Salina and Manhattan, Kansas;

6. These dockets will remain open until further order of the Department; and

7. We will serve copies of this order on the Mayors and airport managers of Salina and Manhattan, Kansas, the Governor of Kansas, the Kansas Department of Transportation, Aviation Division, Mesa Air Group, Inc., Air Midwest, Inc., and Multi-Aero, Inc, d/b/a Air Choice One.

By:

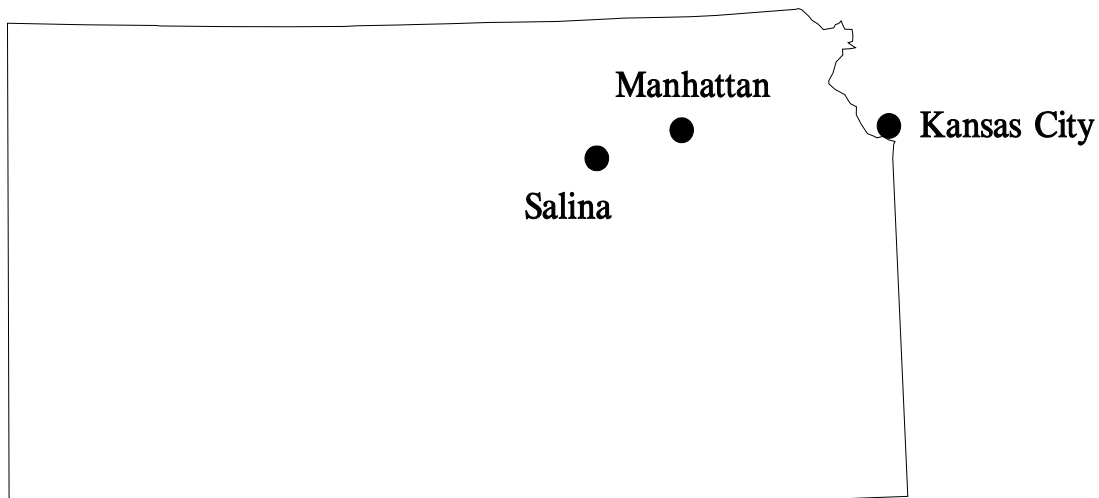
KARAN K. BHATIA
Assistant Secretary for Aviation
and International Affairs

(SEAL)

*An electronic version of this document is available on the World Wide Web at
<http://dms.dot.gov>*

⁸ See Appendix B for the calculation of this rate, which assumes the use of the aircraft designated. If the carrier reports a significant number of aircraft substitutions, a revision of this rate may be required.

AREA MAP



**Air Midwest, Inc., d/b/a US Airways Express
Essential Air Service to be Provided at Salina and
Manhattan, Kansas**

Effective period: Two-year period beginning on the first day of the month following the service date of this order.
Service at
Manhattan: 18 nonstop round trips per week to Kansas City, Kansas.
Service at Salina: 18 nonstop or one-stop round trips per week, via Manhattan, to Kansas City, Kansas.
Intermediate stops and upline service: No other service to any intermediate or upline points is contemplated under the terms of this proposal; accordingly, no such service may be provided on subsidized flights without prior Department approval.
Timing of Flights: Flights must be well-timed and well-spaced to ensure full compensation.
Aircraft type: Beech 1900-D turboprop aircraft (19 passenger seats).

Combined Subsidy Rate per Flight: \$200.78¹

Weekly Compensation Ceiling: \$14,456.16²

Note: The carrier understands that it may forfeit its compensation for any flights that it does not operate in conformance with the terms and stipulations of the rate order, including the service plan outlined in the order and any other significant elements of the required service, without prior approval. The carrier understands that an aircraft take-off and landing at its scheduled destination constitutes a completed flight; absent an explanation supporting subsidy eligibility for a flight that has not been completed, such as certain weather cancellations, only completed flights are considered eligible for subsidy. In addition, if the carrier does not schedule or operate its flights in full conformance with this order for a significant period, it may jeopardize its entire subsidy claim for the period in question. If the carrier contemplates any such changes beyond the scope of the order during the applicable period of these rates, it must first notify the Office of Aviation Analysis in writing and receive written approval from the Department to be assured of full compensation. Should circumstances warrant, the Department may locate and select a replacement carrier to provide service on these routes. The carrier must complete all flights that can be safely operated; flights that overfly points for lack of traffic will not be compensated. In determining whether subsidy payment for a deviating flight should be adjusted or disallowed, the Department will consider the extent to which the goals of the program are met and the extent of access to the national air transportation system provided to the community.

If the Department unilaterally, either partially or completely, terminates or reduces payments for service or changes service requirements at a specific location provided for under this order, then, at the end of the period for which the Department does make payments in the agreed amounts or at the agreed service levels, the carrier may cease to provide service to that specific location without regard to any requirement for notice of such cessation. Those adjustments in the levels of subsidy and/or service that are mutually agreed to in writing by the parties to the agreement do not constitute a total or partial reduction or cessation of payment.

Subsidy contracts are subject to, and incorporate by reference, relevant statutes and Department regulations, as they may be amended from time to time. However, any such statutes, regulations, or amendments thereto shall not operate to controvert the foregoing paragraph.

¹ \$721,605 compensation, divided by 3,594 one-way completed departures, calculated as follows: 36 flights per week * 52 weeks * 96% completion factor * 2 = 3,594 flights.

² Total of 72 flights per week * \$200.78 = \$14,456.16.

Air Midwest, Inc., d/b/a US Airways Express
Proposal to Provide Subsidized EAS at Salina and Manhattan, Kansas
Calculation of Annual Subsidy Requirement

Nonstop Miles: MHK – MCI = 107 miles; SLN – MHK = 59 miles;	
Total Round Trip Miles = 166; Average Stage Length = 83 miles. ¹	166
Weekly Round Trip Service (18 weekly departures @ SLN and MCI; 72 @ MHK)	18 Nonstops
Block Hours (Average Block Time = 1.1 hours per flight or 66 minutes per flight)	1,977 ²
Weighted Departures (3,744 @ 96% completion factor)	3,594
Turns at Hub	898.5
Revenue Passenger Miles (RPMs)	2,304,310
Available Seat Miles (ASMs)	5,668,116
Passengers: SLN – MCI = 4,535; MHK – MCI = 14,500	19,035
Fare: SLN – MCI = \$86.00; MHK – MCI = \$82.50	\$86.00
Passenger Revenue	\$1,588,260
<u>Other Revenue (1% of Passenger Revenue)</u>	<u>15,863</u>
Total Revenue	\$1,602,123
<u>Direct Expenses:</u>	
Crew and Training @ \$153.15 per Block Hour	\$302,752
Hull Insurance @ \$6.93 per Block Hour	13,699
Fuel & Oil @ \$140.00 per Block Hour ³	276,756
Maintenance @ \$239.22 per Block Hour	571,739
Aircraft Rental @ \$49.12 per Block Hour	<u>97,102</u>
Total Direct Expenses	\$1,262,049
<u>Indirect Expenses:</u>	
Traffic @ \$0.060 per RPM	\$231,349
Marketing @ \$5,000 per community	10,000
Capacity (Departure) Related @ \$148.06 per departure	532,163
Capacity (ASM) Related @ \$0.0194 per ASM	109,961
Total Indirect Expenses	<u>\$883,473</u>
Operating Expenses:	\$2,145,522
<u>Return @ 5%</u>	<u>\$107,276</u>
Total Operating Expenses:	<u>\$2,252,798</u>
Operating Profit (Loss)	(\$650,676)
Interest Expense @ \$35.88 per Block Hour	<u>\$70,929</u>
Annual Subsidy	<u>\$721,605</u>
Subsidy per weighted departure	<u>\$200.78</u>
Maximum subsidy per week	<u>\$14,456.16</u>

¹ Salina = SLN; Manhattan = MHK; and Kansas City International = MCI)

² 36 flights per week x 66.0 minutes x 52 weeks x 96% = 118,610 minutes / 60 = 1,977 Block Hours; 3,594 departures.

³ 136 gallons per Block Hour @ \$1.029412 per gallon including oil = \$140.00 per Block Hour.